

Trusts in Financial and Gift Planning

Maximizing Your Benefits



The Benefits of Trusts

A trust can produce beneficial results in your estate and gift planning. In many cases, a trust can add significantly to the financial security you want to provide for your family and loved ones. Trusts can help to save on estate taxes and probate costs and often can produce meaningful income tax savings. Most important, trusts can enable you to control the use and disposition of property for many years after your death.

A trust can also provide the opportunity to make major gifts to important philanthropic causes without reducing either your personal income or the security you want to provide for your family. Indeed, a charitable trust can increase your income, provide tax benefits, and add to the security of your beneficiaries.

However, trusts can have some drawbacks: they could be expensive to create, and, sometimes, to administer. In this booklet, we will outline some of the major advantages and disadvantages of trusts and the tremendous flexibility they can bring to your planning.

What Is a Trust?

A trust is an agreement between you and your trustee. You transfer legal ownership of specified properties to the trustee. The trustee then invests and disposes of the properties according to the agreement.

Clearly, the trust agreement is the foundation for the whole arrangement. Drafted by your attorney, the trust agreement:

- defines how the trustee is to invest the property;
- provides directions for the payment or accumulation of income earned by the trust;
- names one or more immediate beneficiaries and defines their exact benefits and rights;
- directs how long the trust is to last and exactly how the trust property is to be distributed when the trust term ends;
- defines the rights of all beneficiaries and the rights and obligations of the trustee; and
- if the trust is created during your life, the agreement defines your rights to change or modify the agreement, to receive income or other distributions, to change the trustee, etc.

In short, the trust agreement is a specific plan for the management, investment, and use of the trust property. Each trust agreement is written to accomplish the specific objectives of the person creating the trust. Taking the time to plan and draft the trust agreement, to choose the right person to serve as trustee, and to provide flexibility to meet changing conditions and circumstances are keys to a successful trust plan.

Let's first discuss "testamentary" trusts — trusts created by will; then revocable and irrevocable trusts created during life.

A Trust in Your Will

In your will you can direct that all or part of your estate be held in trust for specified family members or other beneficiaries. For example, rather than leaving property outright to your spouse, your will can direct that the property be held in trust for the benefit of your spouse for his or her life, and distributed equally among your children at the death of your spouse.

Whatever provisions you make, the trustee will receive the property at your death. The trustee will technically own the property, but income and principal will be used for your beneficiaries in exact accordance with the directions set forth in the trust document.



What can a testamentary trust accomplish for your beneficiaries? First, it can free your spouse or other beneficiaries from investment and management responsibilities.

Second, a trust created by your will permits you to determine the ultimate beneficiaries of your estate.

Third, a trust permits you to control how your beneficiaries will use and enjoy your property. In your trust agreement (activated through your will), you can provide that your immediate beneficiaries are to receive a specified amount, or the income produced by the trust, or income and whatever amounts of principal are requested or needed by the beneficiaries.

In short, you can provide very broad or very narrow benefits for the trust beneficiaries. Further, you can name several beneficiaries — even give the trustee discretion to “sprinkle” income among the beneficiaries as their needs vary.

It is impossible to say what constitutes a typical trust arrangement. Your beneficiaries may be minors, spendthrifts, elderly, wealthy, comfort-

able, or wholly dependent upon trust income for their support. The directions to the trustee for making distributions to your beneficiaries should be based on all factors — including your own objectives and preferences.

This much is clear: With a carefully planned and drafted trust you can accomplish specific objectives almost as effectively as during your life.

Compare creating a trust to making outright bequests. Which will be better for your family? Which will better accomplish your personal objectives?

Do keep in mind that in your will you can create a trust that will provide a good income to a family member for life and a deferred gift to our institution. You also can create a trust that will provide an annual income to our institution for a number of years, with the property passing to family members at the end of the specified number of years. This permits you to pass your estate to family members sheltered in whole or in part from federal estate taxes.



The Living Revocable Trust

The living revocable trust is created during your life primarily to control the disposition of your estate after your death. It is very much like a testamentary trust and offers virtually the same advantages. In addition, because the trust is created during your life, it provides other features that may make it attractive in your estate planning.

Many people prefer to create trusts during their lives rather than through their wills. Typically, the creator of a living revocable trust reserves the right to receive all the trust income during his or her life, to add or remove property from the trust, and to modify or cancel the whole trust arrangement at any time. In other words, your living revocable trust is completely changeable by you at any time during your life; but at your death, it can become a permanent, irrevocable plan for the management and disposition of your estate.

Example: Bob has created a living revocable trust that is fairly typical. His reasons for creating the trust illustrate some of the features that have made the living revocable trust such a popular planning tool.

Step One: Working with his attorney, Bob developed a comprehensive plan for the disposition of his estate. His major concern is to provide financial security for his wife Anne. To accomplish this, his trust agreement provides that after his death all trust income is to be paid to Anne for as long as she may live. In addition, Anne is to be paid as much principal as she needs for her health, support and maintenance. The trustee is given discretion to handle Anne's financial affairs in the event of her illness or incapacity. The trustee also is authorized to pay certain amounts from the principal to any of Bob's children to meet emergency financial needs. At Anne's death, the trust property is to be divided equally among the children.

Step Two: Most of Bob's investments and other assets are transferred to the trust. The trust is named as the beneficiary of Bob's life insurance and retirement plan benefits. Bob has reserved the right to change the terms or to cancel the arrangement at any time.

It is important to note that even though most of Bob's assets are legally owned by the trust, Bob is in full control. In fact, in many cases, the creator of the trust serves as trustee (a successor trustee is named to take over in the event of his death or incapacity). But even if the creator is not the trustee, his right to change the terms or cancel the trust agreement gives him complete control.

There are four basic reasons for creating his living revocable trust rather than creating the trust through his will:

1. **To minimize probate costs at death.** Properties transferred to the trust during life are not usually part of the probate estate and not subject to probate at death. The savings often can be substantial.
2. **To ensure property will be productive and available to family immediately after death.** Property passing through probate can be tied up for months or even years. But property owned by the trust is not subject to the same probate delays. Present investments are continued and both income and principal are immediately available to distribute under the terms of the trust.
3. **Estate plan avoids public scrutiny.** Unlike a will, which becomes a matter of public record once it enters probate, the trust agreement is private and not available for public examination.
4. **Freedom from day-to-day investment and management responsibilities.** Most important, one knows his or her financial affairs will be prudently handled in the event of death, disability or incompetence.

Estate Tax Consequences

Neither the testamentary trust nor the living revocable trust will reduce federal estate taxes at the creator's death. Properties passing to either form of trust are includible in the creator's gross estate for federal estate tax purposes. However, both forms of trust can avoid a federal estate tax at the death of a trust beneficiary. This can be a very important reason for considering the use of trusts in your personal estate planning. To understand how trusts can save taxes, let's look at some of the basics of our federal estate tax laws.

When a person dies, the fair market value of everything he or she owns is subject to federal estate tax to the extent the value of the estate exceeds an "exemption amount."

Property left outright to a family member is, of course, subject to an estate tax at the death of the family member. But if the property is left in a trust for the benefit of the family member

(and the trust is properly drafted as an irrevocable trust) the value of the trust will not be subject to estate taxation at the death of the beneficiary, even though the benefits are broad and substantial.

Note: Property passing to your spouse is not subject to the estate tax at your death. However, it can be taxed at the death of your spouse. A trust set up for the primary benefit of a spouse can add to the financial security of the spouse and also result in significant estate tax savings. This is a technical area of the law beyond the scope of this booklet, but the avoidance of successive estate taxes is a feature of which you should be aware if you and/or other family members have estates of substantial value.



The Benefits of a Charitable Remainder Trust

Throughout this booklet, we have emphasized how trusts can benefit you and your family. A special kind of trust — the charitable remainder trust — allows you to benefit qualified charitable organizations as well as family members, and may even enhance your tax and financial benefits when technical legal requirements are met.

You, as the donor and the creator of the charitable remainder trust, can gain:

- An increased annual income.
- An income that will be paid to you for life.

- An immediate and substantial income tax charitable deduction.
- Freedom from investment worries and responsibilities.
- The avoidance of an immediate capital gains tax when you transfer appreciated property to a charitable remainder trust.

Family members also can be given a lifetime income from the trust and will enjoy greater financial security because of reduced probate costs, state inheritance taxes, and federal estate taxes.

In your trust agreement, you would name our institution as the remainder beneficiary. We will eventually receive all the trust property left in the trust after income payments to you and family members are completely satisfied.

In many cases, a charitable remainder trust can be an excellent planning tool for you and your family, as well as a means of making a generous future gift that can help shape the future of our institution.

Let Us Hear from You

We will be pleased to discuss the various trust forms with you and to answer your questions. Of course, it is always prudent to have your own attorney or advisor help plan and draft the trusts that can be so important in your planning.

We hope, of course, that you will want to remember us in your plans. We can help you plan a charitable bequest or trust that will provide you with both the greatest tax and financial benefits and the greatest personal satisfaction for you.

Please call us if you have questions or if you would like more information about a trust that can benefit you, your family, and our institution. There is, of course, no cost or other obligation for this service.

